



**JAMES E. "JIM" KING, JR.**  
*President of the Senate*

**THE FLORIDA LEGISLATURE**  
**JOINT SELECT COMMITTEE ON**  
**WORKERS' COMPENSATION RATING REFORM**

**Location**  
 330 Knott Building

**Mailing Address**  
 404 South Monroe Street  
 Tallahassee, Florida 32399-1100  
 (850) 487-5361

Brian Deffenbaugh, *Staff Director*  
 Legislature's Website: [www.leg.state.fl.us](http://www.leg.state.fl.us)



**JOHNNIE BYRD**  
*Speaker of the House of*  
*Representatives*

November 18, 2003

The Honorable James E. "Jim" King, Jr.  
 President, The Florida Senate  
 Suite 409, The Capitol  
 Tallahassee, FL 32399-1100

The Honorable Johnnie Byrd  
 Speaker, The Florida House of Representatives  
 Suite 420, The Capitol  
 Tallahassee, FL 32399-1100

Dear Mr. President and Mr. Speaker:

We are pleased to transmit this letter to you which contains the report and recommendations of the Joint Select Committee on Workers' Compensation Rating Reform. The Joint Select Committee was appointed pursuant to Section 40 of Chapter 2003-412, L.O.F., to study the merits of requiring each workers' compensation insurer to individually file its expense and profit portion of a rate filing, while permitting each insurer to use a loss cost filing made by a licensed rating organization. The committee was also charged with studying other rating options that would promote greater competition and would encourage insurers to write workers' compensation while protecting employers from rates that are excessive, inadequate, or unfairly discriminatory. The Joint Select Committee has taken great care to follow this charge and has sought input from the various stakeholders involved.

The Joint Select Committee on Workers' Compensation Rating Reform met three times during October and November. The committee heard testimony and received written information from the Office of Insurance Regulation, the National Council on Compensation Insurance (NCCI), and interested parties.

### Findings

Florida is one of 8 states that continues to use what is known as an “administered pricing” system under which a rating bureau or statistical agency files the full workers’ compensation rate, subject to the prior approval of the insurance regulatory agency which, in Florida, is the Office of Insurance Regulation. In comparison, 37 states have adopted a “loss cost” system under which a rating bureau or statistical agency files the portion of the rate that is needed to pay losses and, typically, the loss adjustment expenses associated with adjusting and defending specific claims, while each insurer must independently file a “loss cost multiplier” that reflects the insurer’s general expense and profit portion of the rate. The trend among states in recent years has been to move from an administered pricing system to a loss cost system and similar variations intended to rely more heavily on competitive market forces in the setting of workers’ compensation rates.

A loss cost system seeks to promote competition among insurers and maximize benefits to consumers. The National Association of Insurance Commissioners adopted the Property and Casualty Model Rating Law (1998) which provides for a loss cost system under both the prior approval version and file and use version of the model law. The potential disadvantages are the increased risk of inadequate, excessive, or unfairly discriminatory rates and increased administrative costs to the system. The Joint Select Committee found no empirical evidence from testimony and materials presented indicating that the adoption of a loss cost rating system would significantly affect rates or underwriting results. A comparison of the rates and insurer loss ratios among the states displayed no particular pattern among those states that adopted a loss cost system as compared to states with an administered pricing system.

Concern was expressed that this would not be an optimal time for Florida to change to a loss cost rating system by the Office of Insurance Regulation (OIR) and interested parties, although the director of OIR testified in favor of moving towards a more competitive rating law. This concern was primarily due to the recent enactment of major changes to the workers’ compensation law in Senate Bill 50-A, the effects of which are still largely unknown, but which resulted in the filing and approval of a 14 percent rate reduction effective October 1 of this year. Carriers are also undergoing system changes to adapt to the administrative and benefit changes of the new law. Concerns about changing the rating law were also due to the alleged instability of the insurance market, as evidenced by difficulties in obtaining coverage and the growth in the number of employers forced to obtain coverage from the insurer of last resort, the Florida Workers’ Compensation Joint Underwriting Association. The Joint Select Committee heard testimony, primarily anecdotal in nature, on whether the current regulatory environment creates and maintains market conditions that are conducive to competition in the workers’ compensation market.

The current Florida law and the rating plans approved by OIR allow for various ways for insurers to vary or adjust premiums, including retrospective rating plans that adjust the

premium at the end of the policy period to reflect the actual loss experience of the employer; dividend plans that allow insurers to provide refunds to participating policyholders; and premium credits for large deductible policies, approved safety programs, drug-free workplaces, and other standard credits. Florida's use of such aforementioned pricing methods appears to be consistent with their use in other states.

But, certain other rating methods that vary rates among insurers and employers are used less frequently in Florida, compared to other states. Florida law permits insurers to file for approval of a rate deviation, by which the insurer proposes a uniform percentage increase or decrease to be applied to all rates charged or to rates for a particular class or classes of insurance. Deviations have been used very infrequently in Florida since 1996 when legislation (ch. 96-405, L.O.F.) revised the standards for approval and disapproval of deviation filings by the Department of Insurance (now, OIR). In addition to consideration of factors related to the actuarial soundness of the deviation filing, as are considered for rate filings generally, the law requires OIR to consider "the impact of the deviation filing on the current market conditions including the composition of the market, the stability of rates, and the level of competition in the market." The OIR is specifically required to disapprove a deviation filing if it finds the resulting premiums "would adversely affect current market conditions including the composition of the marketplace, the stability of rates, and the level of competition in the market, or would result in predatory pricing." [s. 627.211(3), F.S.]

In contrast, the rate filing standards in Florida for other lines of property and casualty insurance, as well as for deviation filings for workers' compensation in most other states, provide for disapproval of rates that are excessive, inadequate, or unfairly discriminatory. This is primarily a function of the insurer's own loss and expense factors, although some state laws (similar to a version of the NAIC model law) provide that rates cannot be considered excessive if a competitive market exists. Florida may be unique, or is at least in a distinct minority of states, in effectively using market conditions and the stability of rates as grounds for denying a rate decrease. This is more typically based on a finding that a rate is inadequate, defined in s. 627.062(2)(e), F.S., as being clearly insufficient, together with investment income, to sustain projected losses and expenses in the class of business to which they apply.

Another Florida law that allows some flexibility in rating is the "consent to rate" law (s. 627.171, F.S.) which allows an insurer to use a rate in excess of its filed rate on any specific risk (employer) with the written consent of the insured. However, an insurer may not use excess rates pursuant to this law for more than 10 percent of its commercial insurance policies written or renewed in each calendar year for any line of commercial insurance.

In recent months, an increasing number of employers have been forced to obtain coverage from the Florida Workers' Compensation Joint Underwriting Association (FWCJUA), the insurer of last resort. Premiums for coverage in the FWCJUA are typically three to four times as costly as premiums charged by insurers in the voluntary

market. The 2003 workers' compensation act imposed a premium cap in the FWCJUA of 125 percent of the standard rate for small employers with 15 or fewer employees and an experience modification factor of 1.10 or less. However, these policies are assessable, so if the premium turns out to be inadequate, policyholders will be assessed an additional amount to fund the deficit. In fact, all policies sold by the FWCJUA are subject to either assessment or increased renewal premiums to cover all claims and expenses of the FWCJUA, since the law was amended in 1993 to eliminate assessments against carriers in the voluntary market to fund FWCJUA deficits. Insurers may be willing to offer coverage to an employer in the FWCJUA at a premium above the insurer's filed rate on a consent to rate basis, but may not do so for more than 10 percent of an insurer's policies. This limitation may prevent some employers from electing to purchase coverage from an insurer at a rate in excess of the standard rate, but would allow the employer to avoid having to purchase an assessable policy.

### Recommendations

After hearing the testimony and reviewing the written materials, the Joint Select Committee on Workers' Compensation Rating Reform recommends the following:

- Amend s. 627.211, F.S., to revise the standards for approval and disapproval of deviation filings for workers' compensation rates, to be similar to the law as it existed prior to 1996, to provide for disapproval of a filing if it results in premiums that are excessive, inadequate, or unfairly discriminatory. Disapproval of a deviation filing should not be based on factors beyond the loss, expense, and related financial data of the insurer making the deviation filing.
- Amend s. 627.171, F.S., to allow workers' compensation insurers to use rates in excess of their filed rates with the written consent of a policyholder, without being subject to the current maximum limitation of 10 percent of an insurer's commercial policies, for policies issued to employers who the insurer takes out of the Florida Workers' Compensation Joint Underwriting Association. Such employers should be given the option of knowingly and voluntarily accepting such coverage as an alternative to obtaining an assessable policy from the FWCJUA. The Legislature should evaluate additional potential incentives to effect the depopulation of the FWCJUA, such as premium tax credits, Workers' Compensation Administrative Trust Fund assessment abatement, or Special Disability Trust Fund assessment abatement.
- To assist the Legislature in evaluating stability in Florida's market, require the Office of Insurance Regulation to submit an annual report to the Legislature that evaluates competition in the workers' compensation insurance market. The purpose of this annual report is to determine if the state of the market ensures the availability of workers' compensation coverage and affordability of coverage at reasonable levels that are not inadequate, excessive, or unfairly discriminatory. The report would evaluate whether the current market structure, conduct, and

performance are conducive to competition, based upon analysis and economic tests. The Legislature should consider the findings of this report to determine whether any changes to the workers' compensation rating laws are warranted. The report should also document that OIR has complied with the provisions of 627.096, F.S., which requires OIR to investigate and study all workers' compensation insurers in the state and to study the data, statistics, schedules, or other information as it may deem necessary to assist in its review of workers' compensation rate filings.

- Require each workers' compensation insurer to notify the Office of Insurance Regulation in writing of a significant underwriting change that materially limits or restricts the number of policies or premiums written in this state.

The evidence presented to the committee did not demonstrate any obvious benefit or detriment as a result of changing from an administered pricing (full rate) system to a loss cost system. The director of the Office of Insurance Regulation stated that he knew of no evidence that clearly indicated that Florida would be better served under a loss cost system as compared to the current system, and that any such change should not be made until the reforms of Senate Bill 50-A have been in effect for at least 18 months and the insurance market has stabilized. This testimony and the fact that 37 states have adopted a loss cost system, which is also recommended by the NAIC as a way to promote price competition among insurers, leads us to encourage the Legislature to explore such a modification at a time when the impact of SB 50-A and the market stability that it should bring allow for a more conducive environment to revisit such a topic.

We further note that the narrow charge of the committee to make recommendations for changes to the workers' compensation rating laws does not encompass proposals that will significantly address the problems of availability and affordability of the current market. Senate Bill 50-A was intended to address these problems and did result in an immediate reduction in rates averaging 14 percent, but coverage remains difficult to obtain, particularly for small employers. One major insurer has terminated a program covering approximately 4,500 contractors in this state. Many of these non-renewals will take effect January 1, 2004, which will add to the already increasing number of employers who are forced to obtain coverage from the Florida Workers' Compensation Joint Underwriting Association. Even though small employers who meet certain criteria are subject to specified premium caps, those employers remain liable for additional premium assessments if necessary to fund plan losses. The committee recognizes that legislative solutions to these problems are likely to be advanced to address these problems, which were not the subject of our limited review.

Thank you for recognizing the importance of all these issues and for providing a forum for interested parties to participate.

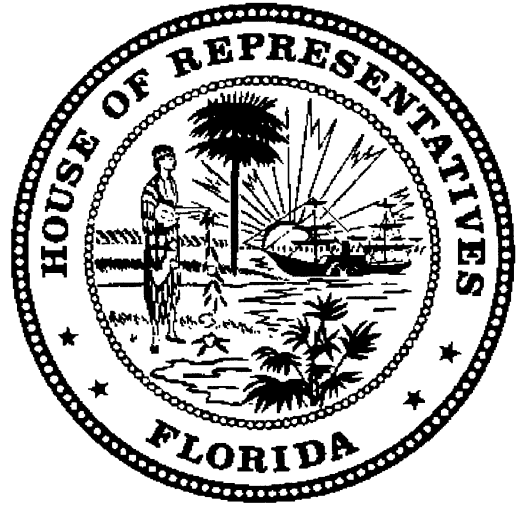
Sincerely,

A handwritten signature in black ink, reading "Jeffrey H. Atwater". The signature is fluid and cursive, with the first name "Jeffrey" being more prominent.

Senator Jeffrey H. "Jeff" Atwater  
Chair

A handwritten signature in black ink, reading "Kimberly Kim Berfield". The signature is fluid and cursive, with the first name "Kimberly" being more prominent.

Representative Kim Berfield  
Vice Chair



# **JOINT SELECT COMMITTEE ON WORKERS' COMPENSATION RATING REFORM**

Senator Jeff Atwater, Chair  
Rep. Kim Berfield, Vice Chair

## **Meeting Packet**

Monday, November 17, 2003

8:15 a.m. – 11:00 a.m.

Room 110, Senate Office Building

***(Please bring this packet to the committee meeting.  
Duplicate materials will not be available.)***

## A G E N D A

### JOINT SELECT COMMITTEE ON WORKERS' COMPENSATION RATING REFORM

DATE: Monday, November 17, 2003

TIME: 8:15 a.m. -- 11:00 a.m.

PLACE: Room 110 (EL), Senate Office Building

#### MEMBERS:

TAB	BILL NO. AND INTRODUCER	BILL DESCRIPTION AND SENATE COMMITTEE ACTIONS	COMMITTEE ACTION
	Senate Membership: Senator Jeffrey H. "Jeff" Atwater, Chair Senator Walter G. "Skip" Campbell Senator Charlie Clary		
	House Membership: Rep. Kim Berfield, Vice Chair Rep. Donald D. "Don" Brown Rep. Dennis A. Ross		
1	Consideration of options to current workers' compensation rating law. --Office of Insurance Regulation response to select committee follow-up questions. --National Council on Compensation Insurance response to select committee follow-up questions.		
2	Adoption of Final Report and Recommendations. --Draft Final Report and Recommendations.		



**JOINT SELECT COMMITTEE ON  
WORKERS' COMPENSATION RATING REFORM  
NOVEMBER 6, 2003**

**10-Nov-03**

**Kevin McCarty, Director, Office of Insurance Regulation  
Committee Questions**

***1. Is Hartford still writing workers' compensation insurance in the Florida market?***

The Hartford has terminated the Florida Home Builders Association program that covered approximately 4,500 employers. Employers in this program are being non-renewed.

In response to an inquiry from the Office of Insurance Regulation (OIR), the Hartford advised,

*"While it would be fair to say we are highly selective and will be non-renewing individual risks and our total volume will be shrinking, we will still be willing to write some new business and will be renewing existing accounts."*

***2. Have any workers' compensation carriers left the market or indicated that they would nonrenew policyholders in 2003 or 2004?***

Carriers are not required by law to notify the OIR when a carrier decides to non-renew a portion of its business in Florida. However, carriers will generally notify OIR of significant underwriting changes that could affect marketing and/or distribution of policies in the State. Over the past several years, the OIR has been informally notified that various carriers intended to limit writing of new business or intended to non-renew policies (see Hartford above, FCCI, CNA, Kemper, Firemen's Fund).

It should be noted that the law, at 624.403, F.S., does require a company to notify the OIR 90 days in advance, if the company intends to withdraw completely from writing a line of business.

*Lack of Availability in the Market*

The availability problem for workers' compensation is created mainly by existing carriers restricting new business writings and non-renewing policies not by carriers completely withdrawing from the market.

To illustrate, from January 1, 2002 to the present, carriers entering or leaving the workers' compensation market can be summarized as follows:

- Since January 1, 2002, fifteen (15) carriers were admitted to Florida or added workers' compensation to the company's line of business being written in Florida;
- Only one carrier -- TIG Premier Insurance Company -- has formally withdrawn its COA to write workers' compensation in Florida. For this company, the formal withdrawal is a reflection of a nationwide restructuring program for this company;
- Five (5) out-of-state carriers and one domestic carrier, Aries Insurance Company, were liquidated; and,
- Eight carriers have been suspended from issuing new policies in Florida.

***3. What period would you characterize as being the last period of stability in the workers' compensation market?***

The period 1997 to 09/11/2001.

***How would you define market stability in terms of the workers' compensation market?***

- The absence of major law changes -- it takes one to two years to see how major changes in the law are going to be implemented by the all affected parties and the period immediately following major law changes is a time of uncertainty;
- A market characterized by rate decreases or modest increases in rates;
- The number of policies in the residual market are a small percentage of the total number of policies in the market;
- There is an absence of court decisions that result in greatly expanding benefits; and,
- There is an absence of major insolvencies or significant market restructuring.

**Explanation of Basis for Selecting 1997 to 09/11/2001**

There was a major law change effective January 1, 1994 that restructured benefits, created FWCJUA, required implementation of managed care by 1/1/1997 and changed regulation of self-insurer funds. During 1994, 1995 and most of 1996, carriers were involved in creating managed care arrangements, implementing new statutory benefits and self-insurer funds were being converted to insurance companies or merging with insurance companies. Thus, it was not until 1997 that there was some stability for employers and carriers.

The FWCJUA began operations on January 1, 1994. The FWCJUA has had the following written premiums:

<u>Calendar Year</u>	<u>Written Premium</u>
2002	\$ 25,645,248
2001	6,696,022
2000	5,035,549
1999	6,431,378
1998	14,182,389
1997	13,862,990
1996	27,748,666
1995	69,102,344
1994	73,305,743

#### NOTES

- For the period 1997 to 2001 the FWCJUA wrote less than 1% of the total market.
- The chart also illustrates that there were significant drops in premium in 1996 and 1997 and a large increase in 2002.

For the period 1997 to 2001, there were decreases or modest increases as illustrated by the history of approved rate changes below:

<u>Date</u>	<u>DOI Approved Change</u>
01-01-1994	-10.6%
01-01-1995	No Filing
01-01-1996	No Filing
01-01-1997	-11.3%
01-01-1998	-1.7%
01-01-1999	1.6%
01-01-2000	2.5%
01-01-2001	0.0%
01-01-2002	0.0%
08-01-2002	2.7%
04-01-2003	13.7%
10-01-2003	-14.0%

For the period 1997 to the present, there have been no significant insolvencies in the Florida market that have adversely affected employer access to coverage.

For the period 1997 to 2001, there was no significant market restructuring affecting companies writing workers' compensation coverage in Florida. In 2002, a major carrier's decision to restrict writing of Professional Employer Organizations (PEOs – otherwise more commonly known as “employer leasing companies”) resulted in market problems for many employers. Also in 2002, several other carriers announced decisions to limit coverage in the Florida market.

The reason for selecting September 11, 2001, as the end of the period of stability is that the terrorist event of 9/11 changed the way carriers looked at workers' compensation and that event

served to heighten concerns that had been developing related to reinsurance, the economy and investment returns.

**4. *What specific recommendations do you have to improve competition in the Florida market?***

*See responses to questions #5 and #6*

**5. *What changes, if any, would you recommend to the statutory provisions relating to deviations?***

The proposed amendments remove the requirement that OIR consider “*composition of market, stability of rates and the level of competition*” in approving rate deviations.

All of these criteria require a subjective judgment component that has made it difficult to administer – both for carriers and for the OIR. Deletion of these criteria references would confine a deviation filing to more objective requirements related to adequate pricing.  
(Draft attached)

**6. *What changes, if any, would you recommend to the consent to rate statutory provisions?***

Current law, at s. 627.171, F.S., prohibits a carrier from entering consent-to-rate agreements with more than 10% of the carrier’s total commercial policies issued or renewed within any one calendar year.

The OIR proposes an amendment that will create an exemption for carriers removing policies from the Florida Workers’ Compensation JUA (FWCJUA) from the limitation of a 10% maximum number of commercial policies issued on a consent-to-rate basis. With this amendment, a carrier could continue to write other commercial risks on a consent-to-rate basis without having these workers’ compensation policies counting “against” the 10% cap.  
(Draft attached)

**NOTE**

There is need for another amendment to s. 627.311, F.S., that will assure that any employer currently insured by the JUA and considering an offer for a consent-to-rate policy, does not lose his/her eligibility for JUA coverage.

## DRAFT LEGISLATION

### *5. What changes, if any, would you recommend to the statutory provisions relating to deviations?*

#### **627.211 Deviations; workers' compensation and employer's liability insurances.--**

(1) Every member or subscriber to a rating organization shall, as to workers' compensation or employer's liability insurance, adhere to the filings made on its behalf by such organization; except that any such insurer may make written application to the office for permission to file a uniform percentage decrease or increase to be applied to the premiums produced by the rating system so filed for a kind of insurance, for a class of insurance which is found by the office to be a proper rating unit for the application of such uniform percentage decrease or increase, or for a subdivision of workers' compensation or employer's liability insurance:

(a) Comprised of a group of manual classifications which is treated as a separate unit for ratemaking purposes; or

(b) For which separate expense provisions are included in the filings of the rating organization.

Such application shall specify the basis for the modification and shall be accompanied by the data upon which the applicant relies. A copy of the application and data shall be sent simultaneously to the rating organization.

(2) Every member or subscriber to a rating organization may, as to workers' compensation and employer's liability insurance, file a plan or plans to use deviations that vary according to factors present in each insured's individual risk. The insurer that files for the deviations provided in this subsection shall file the qualifications for the plans, schedules of rating factors, and the maximum deviation factors which shall be subject to the approval of the office pursuant to s. 627.091. The actual deviation which shall be used for each insured that qualifies under this subsection may not exceed the maximum filed deviation under that plan and shall be based on the merits of each insured's individual risk as determined by using schedules of rating factors which shall be applied uniformly. Insurers shall maintain statistical data in accordance with the schedule of rating factors. Such data shall be available to support the continued use of such varying deviations.

(3) In considering an application for the deviation, the office shall give consideration to the applicable principles for ratemaking as set forth in ss. 627.062 and 627.072, and the financial condition of the insurer, ~~and the impact of the deviation on the current market conditions including the composition of the market, the stability of rates, and the level of competition in the market.~~ In evaluating the financial condition of the insurer, the office may consider: (1) the insurer's audited financial statements and whether the statements provide unqualified opinions or contain significant qualifications or "subject to" provisions; (2) any independent or other actuarial certification of loss reserves; (3) whether workers' compensation and employer's liability reserves are above the midpoint or best estimate of the actuary's reserve range estimate; (4) the adequacy of the proposed rate; (5) historical experience demonstrating the

profitability of the insurer; (6) the existence of excess or other reinsurance that contains a sufficiently low attachment point and maximums that provide adequate protection to the insurer; and (7) other factors considered relevant to the financial condition of the insurer by the office. The office shall approve the deviation if it finds it to be justified, it would not endanger the financial condition of the insurer, ~~it would not adversely affect the current market conditions including the composition of the market, the stability of rates, and the level of competition in the market,~~ and that the deviation would not constitute predatory pricing. It shall disapprove the deviation if it finds that the resulting premiums would be excessive, inadequate, or unfairly discriminatory, would endanger the financial condition of the insurer, ~~or would adversely affect current market conditions including the composition of the marketplace, the stability of rates, and the level of competition in the market,~~ or would result in predatory pricing. The insurer may not use a deviation unless the deviation is specifically approved by the office.

(4) Each deviation permitted to be filed shall be effective for a period of 1 year unless terminated, extended, or modified with the approval of the office. If at any time after a deviation has been approved the office finds that the deviation no longer meets the requirements of this code, it shall notify the insurer in what respects it finds that the deviation fails to meet such requirements and specify when, within a reasonable period thereafter, the deviation shall be deemed no longer effective. The notice shall not affect any insurance contract or policy made or issued prior to the expiration of the period set forth in the notice.

(5) For purposes of this section, the office, when considering the experience of any insurer, shall consider the experience of any predecessor insurer when the business and the liabilities of the predecessor insurer were assumed by the insurer pursuant to an order of the office which approves the assumption of the business and the liabilities.

**6. What changes, if any, would you recommend to the consent to rate statutory provisions?**

627.171 Excess rates.--

(1) With written consent of the insured signed prior to the policy inception date and filed with the insurer, the insurer may use a rate in excess of the otherwise applicable filed rate on any specific risk. The signed consent form must include the filed rate as well as the excess rate for the risk insured, and a copy of the form must be maintained by the insurer for 3 years and be available for review by the office.

(2) An insurer may not use excess rates pursuant to this section for more than 10 percent of its commercial insurance policies written or renewed in each calendar year for any line of commercial insurance or for more than 5 percent of its personal lines insurance policies written or renewed in each calendar year for any line of personal insurance. In determining the 10 percent limitation for commercial insurance policies the insurer shall exclude any workers' compensation policy that was written for an employer who had coverage in the joint underwriting plan created by s. 627.311(5) immediately prior to being written and any workers' compensation policy that was written for an employer that had been offered coverage in the joint underwriting plan but was written by the insurer in lieu of accepting the joint underwriting plan policy. These workers' compensation policies shall be excluded from the 10 percent limitation for the first three years of coverage.

**NCCI RESPONSE TO THE JOINT SELECT COMMITTEE ON  
WORKERS' COMPENSATION RATING REFORM  
FOLLOW-UP QUESTIONS**

1. In full rate states, why does NCCI use countrywide averages for general and production expenses rather than state specific numbers?

For General expense, countrywide data is not available. Carriers do not report state-specific General expense.

Production expense can be separated into two components: (1) commissions and (2) other acquisition costs.

Similar to General expenses, other acquisition costs are not reported on a state-specific basis. Countrywide data is all that is available.

While commissions are available on a state-specific basis, these reported commissions reflect premium discounts (size of policy discounts) as well as contingent commissions that generally vary according to the loss experience of an account. For ratemaking purposes, the premium discounts must be removed from the data. This is more easily accomplished on a countrywide basis, partly because the size of policy depends on many multi-state policies. The contingent commissions would also distort any true state-by-state differences since different loss experience by state might make similar commission scales between states look different.

In addition, large multi-state employers account for the majority of commissions and these commissions are generally paid on the total multi-state premium, not on a state-by-state basis.

One item in Production and General expense that is reported on a countrywide basis is cost to the insurer of running internal operations (eg., rent, salaries). This is not reported on a state-by-state basis because insurers often handle multi-state operations from their headquarters in a particular state. It is not appropriate to allocate all of that expense to the state in which the headquarters is located. Nor is there any easy way to breakout that expense among each state in which the insurer does business. As a result, all insurers report this item on a countrywide basis.

2. How do these countrywide averages compare with the actual general and production expenses for a particular state?



As stated above, the only part of production and general expense available on a state-by-state basis is commission and brokerage expense data.

Attached are several charts which compare those expense items that are available on a state-by-state basis as well as the NCCI state average and Florida's ranking among the NCCI states. The states labeled in green are full rate states. The states labeled in blue are NCCI loss cost states. Given that full rate states are towards each end of the scale in each chart, one cannot conclude that expenses are higher or lower in full rate states as opposed to loss cost states.

One of the attached charts provides commissions by state. As noted in (1), these commissions may reflect different sizes of policy by state and different loss experience and not just different commission scales. These differences would need to be removed for ratemaking purposes.

3. What is the status regarding ongoing litigation involving NCCI as a rating or advisory organization?

The only litigation that NCCI is engaged in due to its capacity as a rating or advisory organization is a matter pending in Arizona. In this case, plaintiffs (which are, for the most part, large, sophisticated corporations) have alleged that the insurance company defendants breached the terms of loss sensitive or retrospectively rated workers compensation insurance policies by including charges and utilizing forms that were not authorized by filings made with insurance regulators. Plaintiffs further alleged that NCCI was negligent in failing to file "forms and rates that were actually being used by the carriers" and approving "carrier-proposed rates for plaintiffs' policies knowing that the carriers were not intending to use such rates." NCCI filed its answer to the Second Amended Complaint in May 2001. The case has been dormant since then. A related case is on file in Palm Beach County, Florida, but it has been stayed for several years.

There were other cases filed with allegations relating to retrospectively rated policies in other states but they have been dismissed.

For further questions, please contact:

**Lori Lovgren**  
**State Relations Executive**  
**NCCI**  
**901 Peninsula Corporate Circle**  
**Boca Raton FL 33487**  
**561-893-3337 (Phone)**  
**561-893-5463 (Fax)**  
**LORI\_LOVGREN@NCCI.COM**

# Components of Expenses/Source of Data

(Note: Expenses available by state in bold)

1. **Direct Defense and Cost Containment Expense<sup>1</sup>** – Includes defense, litigation and medical cost containment expenses.
2. Adjusting and Other Expenses<sup>2</sup> – Reflects the remaining costs associated with the settlement of claims, such as fees of claims adjusters.
3. **Commission and Brokerage Expenses<sup>1</sup>** – **Reflects fees paid by the insurers to agents and brokers who represent the insured in placing orders for coverage.**
4. General and Other Acquisition Expenses<sup>2</sup> – Reflects costs to the insurer of running internal operations (e.g., rent, salaries), general activities (e.g., administration, payroll, audits, boards and bureau funding, and inspections) and other acquisition costs (e.g., advertising and premium collection expenses).
5. **Dividends<sup>1</sup>** – **Reflects dividends as a percentage of earned premium based on individual state information from Statutory Page 14 data of the Annual Statement.**

<sup>1</sup> Calculated by state using data derived from Statutory Page 14 data of the Annual Statement.

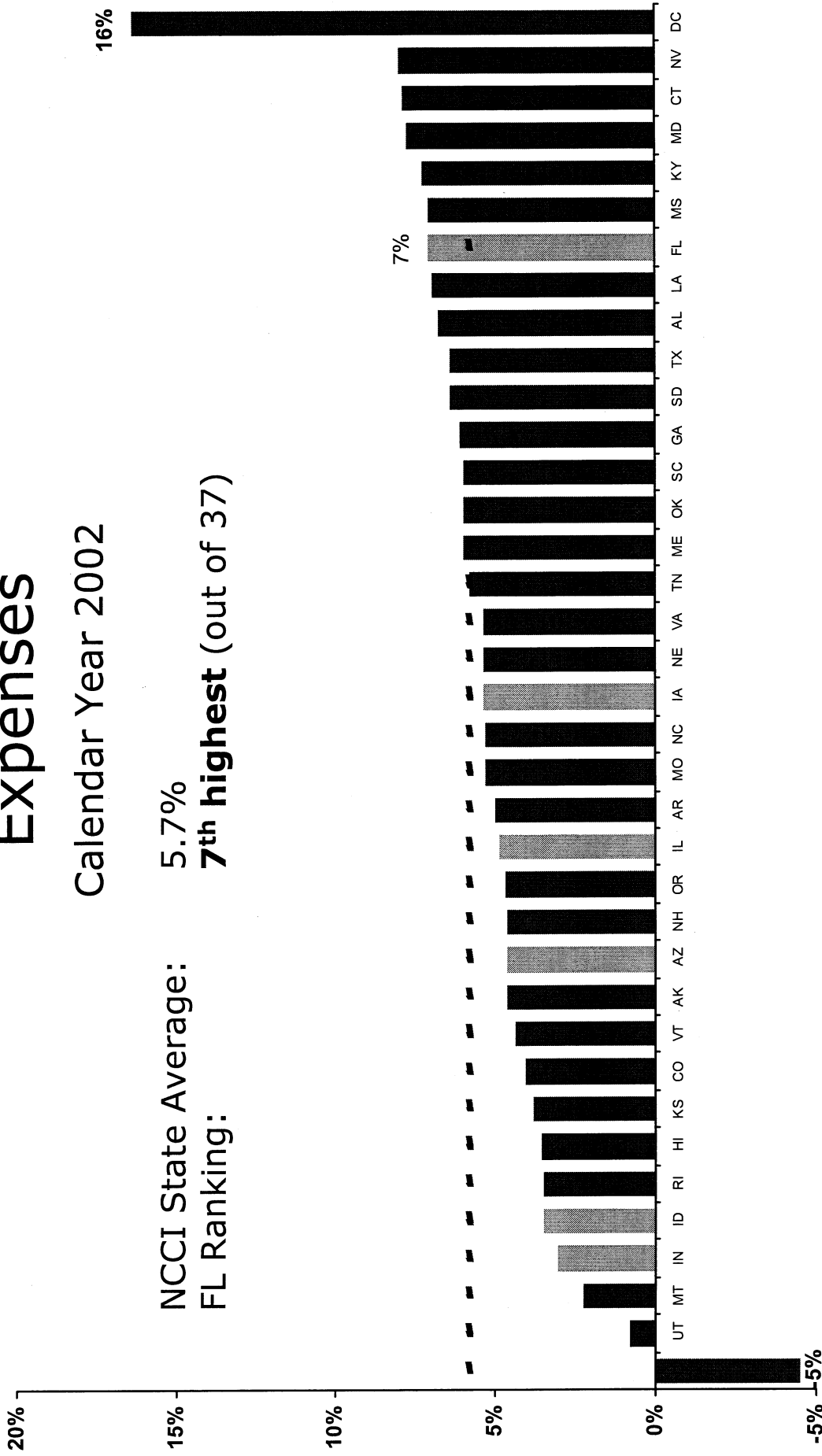
<sup>2</sup> Derived from Insurance Expense Exhibit using countrywide data.

# Direct Defense and Cost Containment Expenses

Calendar Year 2002

NCCI State Average: 5.7%

FL Ranking: 7<sup>th</sup> highest (out of 37)

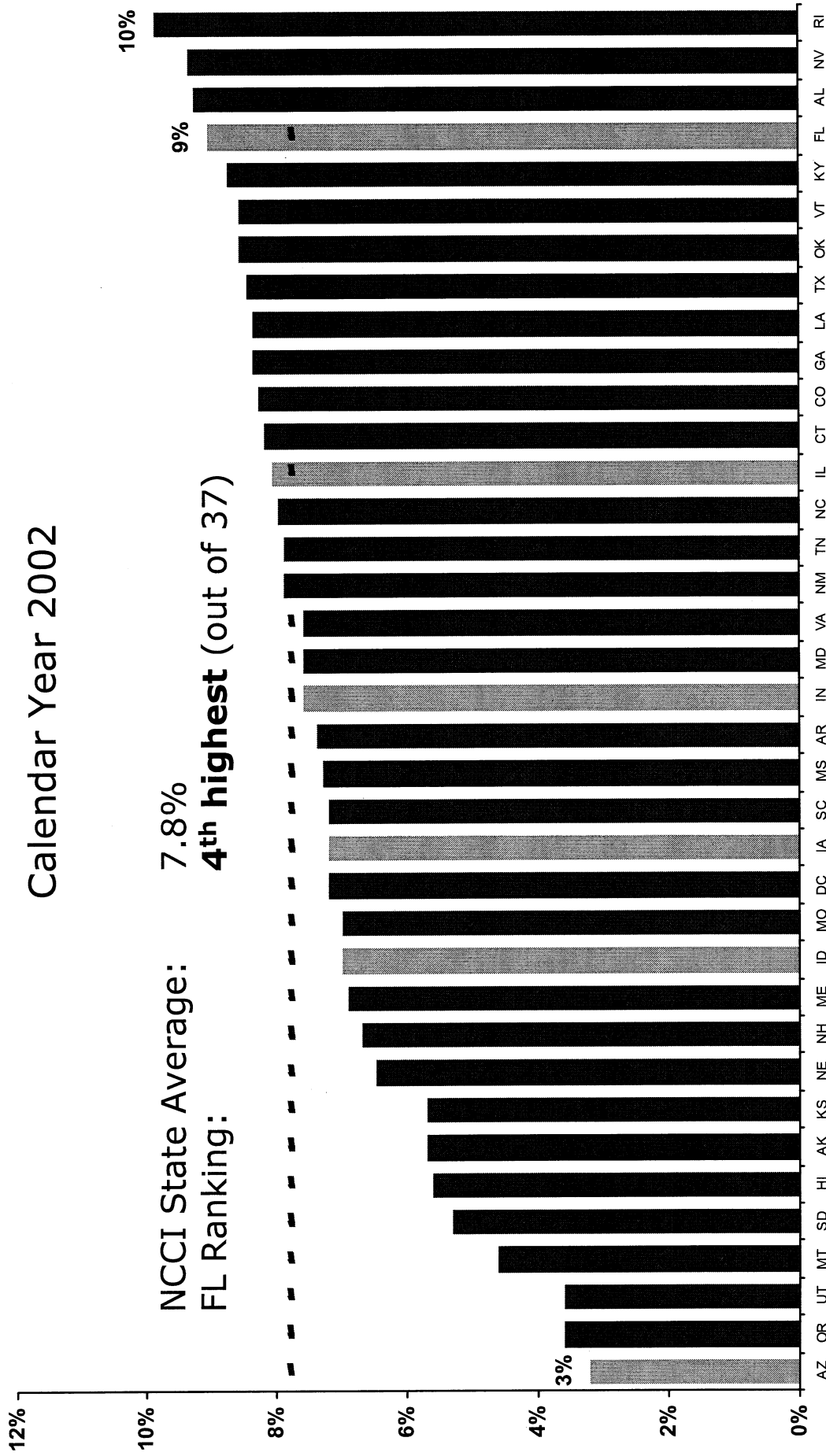


AZ, CO, HI, KY, LA, ME, MO, MT, NM, OR, RI, TX, and UT contain data for a state fund. All other states include private carriers only.



# Commission and Brokerage Expenses

Calendar Year 2002

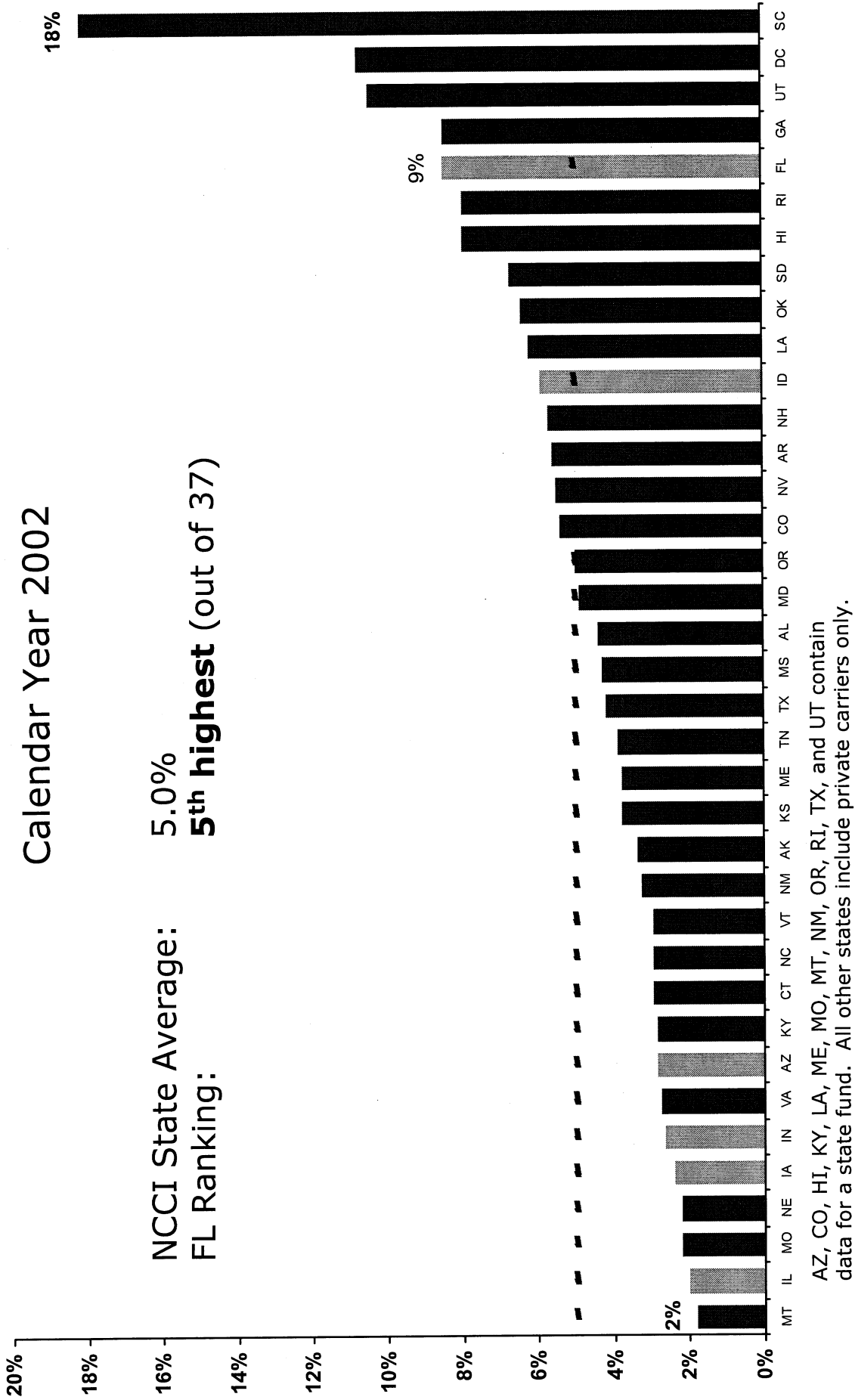


AZ, CO, HI, KY, LA, ME, MO, MT, NM, OR, RI, TX, and UT contain data for a state fund. All other states include private carriers only.



# Taxes, Licenses and Fees

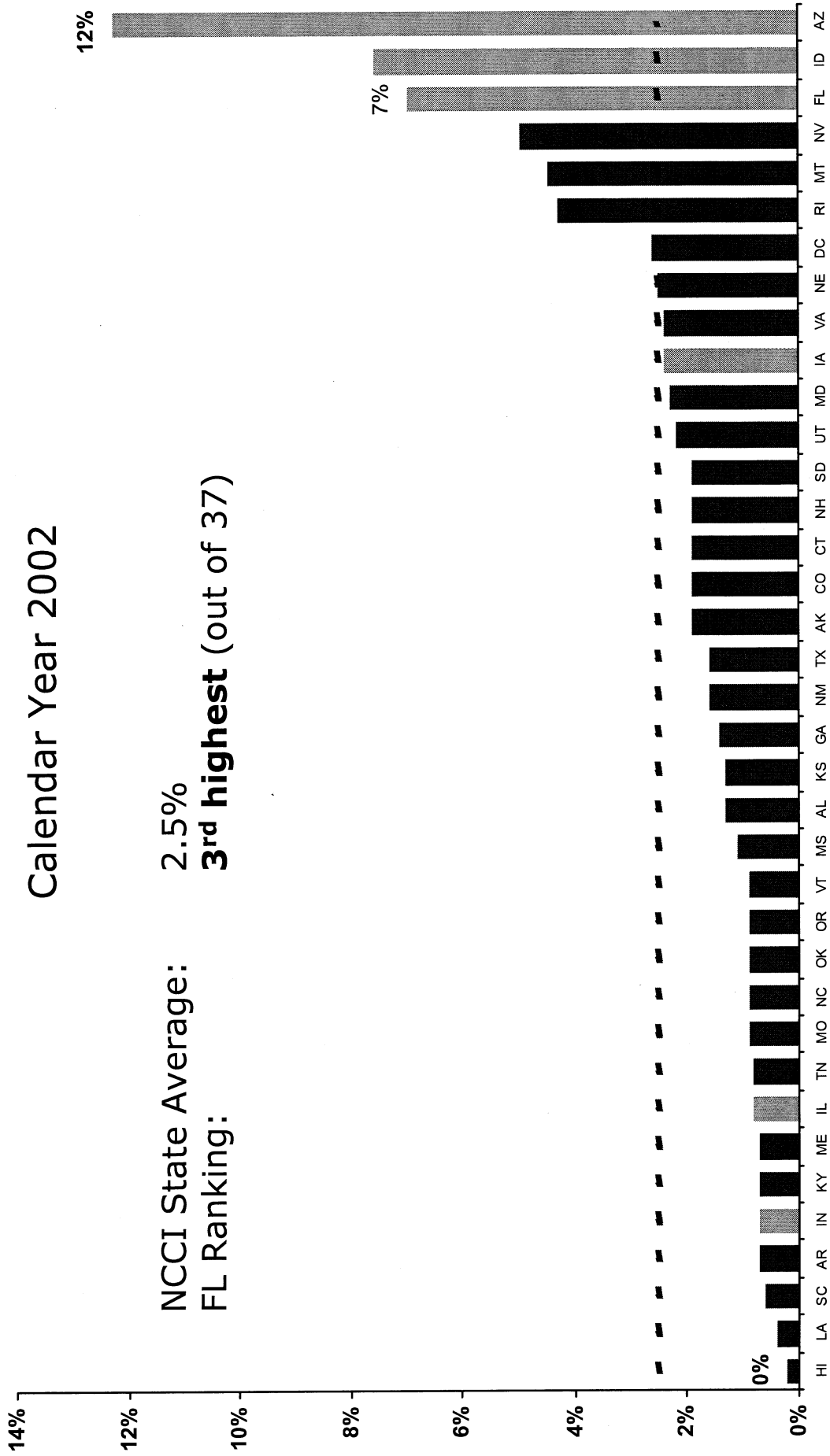
Calendar Year 2002



# Dividends

Calendar Year 2002

NCCI State Average: 2.5%  
 FL Ranking: 3<sup>rd</sup> **highest** (out of 37)



AZ, CO, HI, KY, LA, ME, MO, MT, NM, OR, RI, TX, and UT contain data for a state fund. All other states include private carriers only.

